



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 3A
THE INSOLVENCY SYSTEM OF THE UNITED STATES

This is the **summative (formal) assessment** for **Module 3A** of this course and is compulsory for all candidates who **selected this module as one of their compulsory modules from Module 3**. Please read instruction 6.1 on the next page very carefully.

If you selected this module as **one of your elective modules**, please read instruction 6.2 on the next page very carefully.

The mark awarded for this assessment will determine your final mark for Module 3A. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in MS Word format, using a standard A4 size page and a 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentID.assessment3A]**. An example would be something along the following lines: 202122-514.assessment3A. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words "studentID" with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
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- 6.1 If you selected Module 3A as one of your **compulsory modules** (see the e-mail that was sent to you when your place on the course was confirmed), the final time and date for the submission of this assessment is **23:00 (11 pm) GMT on 1 March 2022**. The assessment submission portal will close at 23:00 (11 pm) GMT on 1 March 2022. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
- 6.2 If you selected Module 3A as one of your **elective modules** (see the e-mail that was sent to you when your place on the course was confirmed), you have a **choice** as to when you may submit this assessment. You may either submit the assessment by **23:00 (11 pm) GMT on 1 March 2022** or by **23:00 (11 pm) BST (GMT +1) on 31 July 2022**. If you elect to submit by 1 March 2022, you **may not** submit the assessment again by 31 July 2022 (for example, in order to achieve a higher mark).
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

ANSWER ALL THE QUESTIONS

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QUESTION 1 (multiple-choice questions) [10 marks in total]

Commented [H(2): Total marks 9/10

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Question 1.1

Commented [H(3): Correct, 1 mark

ABC Corp is filing for bankruptcy under chapter 11. Which of the following **is not** a party in interest in that proceeding?

- (a) A neighboring land owner who has leased equipment to ABC Corp.
- (b) ABC's government regulator.
- (c) A bank that has loaned money to ABC.
- (d) A local advocacy group.**
- (e) All of the above.

Question 1.2

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Which of the following statements regarding executory contracts is **false**?

- (a) Executory contracts are clearly defined by the bankruptcy code.**
- (b) Chapter 11 debtors have greater flexibility than chapter 7 debtors on when they may assume, assign or reject an executory contract.
- (c) In the most common formulation, executory contracts are defined as those where both sides to a contract have material unperformed obligations.
- (d) A court will generally defer to a debtor's business judgment regarding whether to assume or reject an executory contract.
- (e) Under the hypothetical test, a debtor cannot assume an executory contract if the debtor could not also assign the contract.

Question 1.3

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In which of the following scenarios does a bankruptcy court have constitutional authority to issue a final order? Assume in each that the counterparty to the dispute has not consented to the bankruptcy court's exercise of jurisdiction.

- (a) A counterclaim against the estate that introduces a question under state law.
- (b) Since the list of core proceedings is non-exhaustive, a bankruptcy court may issue a final determination on any matter that comes before it.

(c) A creditor's claim against an affiliate of the debtor that has guaranteed the debtor's obligation to the creditor

(d) A debtor's motion to dismiss an involuntary bankruptcy petition.

(e) None of the above.

Question 1.4

Which of the following statements about "pre-packs" is **false**?

(a) A pre-pack cannot be used if the debtor wishes to reject executory contracts.

(b) Creditors must have sufficient information about the debtor and the plan to make an informed voting decision.

(c) A pre-pack debtor may spend as little as a single day in bankruptcy.

(d) The proposed plan of reorganization is submitted to the bankruptcy court together with the voluntary petition.

(e) Creditors' commitment to vote in favor of the plan may be memorialized in a restructuring support agreement.

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Question 1.5

Which of the following statements regarding cramdowns is **true**?

(a) If one insider creditor approves of the plan of reorganization, all other impaired classes may be crammed down.

(b) Because cramdowns do not require the consent of all classes, the plan of reorganization may not be fair and equitable to all impaired classes.

(c) Differential treatment of different classes is permitted if there is a reasonable, good faith basis for doing so and such treatment is required for the plan of reorganization to be successful.

(d) Class definition is rarely a battleground when a debtor tries to cramdown classes.

(e) Dissenting creditors are not permitted to challenge the classification of a creditor supporting the cramdown.

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Question 1.6

Which of the following statements about the plan exclusivity period is **true**?

(a) The exclusivity period is 1 year.

(b) The exclusivity period cannot be extended.

(c) The exclusivity period cannot be shortened.

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(d) During the exclusivity period, only a creditor may propose a plan of reorganization.

(e) During the exclusivity period, only the debtor may propose a plan of reorganization.

Question 1.7

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Which of the following statements about chapter 15 is **false**?

(a) The automatic stay applies upon the filing of a petition for recognition.

(b) A debtor cannot be subject to an involuntary chapter 15 proceeding.

(c) A chapter 15 petition must be filed by a foreign representative.

(d) The automatic stay applies only to property within the territorial jurisdiction of the United States.

(e) Recognition may be granted to a foreign proceeding as either foreign main or foreign non-main.

Question 1.8

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Which of the following statements about 363 sales is **false**?

(a) A 363 sale permits a debtor to sell an asset free and clear of encumbrances.

(b) A creditor's lien on assets sold in a 363 sale attaches to the proceeds of the sale.

(c) A 363 sale must be conducted as an auction with a stalking horse bidder.

(d) Purchasers may pay a higher price for assets sold in a 363 sale than in an out-of-court transaction.

(e) Sophisticated parties will insist on a 363 sale if there is any question regarding whether the sale is "in the ordinary course of business".

Question 1.9

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If a debtor rejects an executory trademark license agreement under which it licenses a trademark to its counterparty, which of the following is **true**?

(a) The counterparty has a claim for damages for breach of contract.

(b) The counterparty must immediately stop using the trademark.

(c) The counterparty can continue using the trademark for the remaining period of the license.

(d) Both (a) and (b).

(e) Both (a) and (c).

Question 1.10

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Who may serve as a foreign representative to seek recognition of a foreign proceeding under chapter 15?

- (a) The board of directors of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (b) An insolvency professional appointed by a creditor where the foreign proceeding is an involuntary receivership.
- (c) An officer of the debtor if it is a debtor-in-possession in the foreign proceeding.
- (d) An insolvency professional appointed by the court overseeing the foreign proceeding.
- (e) All of the above.

QUESTION 2 (direct questions) [10 marks]

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Question 2.1 (2 marks)

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What is the difference between a voluntary petition for bankruptcy and an involuntary petition for bankruptcy?

Filing a petition for bankruptcy **commences the insolvency proceedings**. Such commencement could occur in two forms, namely through a voluntary or an involuntary petition.

Under **§ 301(a) Title 11 of the U.S. Bankruptcy Code** (henceforth, "*title USC § section*"), a **voluntary petition** is filed by the **debtor entity**. It can be supplemented with schedules containing lists of assets and creditors, or could be filed as a "naked" petition without supplementary information. This petition invokes the automatic stay and commences the proceedings. The debtor does not have to be or claim to be insolvent and may commence the proceeding under any applicable chapter of the Bankruptcy Code.

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Under **11 USC § 303(a)**, an **involuntary petition** is filed by the **creditors**. Certain requirements have to be met to file such a petition.

Commented [H(16)]: Correct, 1 mark

Firstly, the number of creditors required for petitioning the involuntary proceeding depends on the number of total non-contingent and non-insider creditors concerned. Where the debtor has less than twelve of such creditors, only one is sufficient to file a petition. However, if the debtor has twelve or more of such creditors, at least three petitioning creditors are required. To qualify as a petitioning creditor, the signatory needs to have a claim that is (1) non-contingent, meaning that the claim is matured and does not depend on potential future events, (2) not subject of a bona fide dispute regarding liability or amount, meaning that the debtor does not have a subjective belief that the debt is not owed/incorrect/insufficient and there is no objectively reasonable basis for a dispute as a matter of fact or law, and (3) un(der)secured in the amount of at least \$10,000 – this amount changes periodically – either separately or in the aggregate with other creditors' claims. (See **11 USC § 303(b)**)

Secondly, such proceedings can only be commenced against an eligible debtor, ie not a "farmer, family farmer, or a corporation that is not moneyed". (See **11 USC § 303(a)**)

Thirdly, for the commencement of this proceeding, the creditors need to allege the debtor of being insolvent either by claiming that the debtor is generally not paying its debts as they become due or by claiming that within 120 days before the filing of the petition, a custodian was appointed or took possession. (See **11 USC § 303(h)**)

Lastly, and in contrast with the voluntary petition, this petition can only commence a chapter 7 or 11 proceeding. (See **11 USC § 303(a)**)

Question 2.2 (2 marks)

What are two potential consequences of a violation of the automatic stay?

Automatic stay: A stay under **11 USC § 362** is automatic, meaning that it comes into effect immediately on the filing of any petition and has a worldwide scope. Its broad scope prohibits several types of interference of the estate under **11 USC § 362(a)**, such as litigating pre-petition claims or enforcing pre-petition judgments against the debtor.

Potential Consequences: If an act is taken in breach of the stay, the act will be considered **void or voidable**. This depends on the circuit in which the proceeding is taking place. However, the violators may attempt to **lift the stay** in order to ensure that the violation is retroactively validated by the court.

If the sought relief is not permitted, the violation may result in the imposition of **contempt sanctions**, ie sanction because the stay violator committed the offence of being disobedient to a law. This could include the payment of the debtor's lawyer fees and the undoing of the acts that change the status quo of the estate's property. If the violator does not act promptly, the court may impose **coercive contempt sanctions** such as daily fines until rectification of the violation.

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Question 2.3 (3 marks)

In what circumstances is a claim considered "impaired"? When is a holder of an impaired claim not entitled to vote on a proposed plan of reorganization and what happens instead?

When formulating a reorganization plan under Chapter 11 of the US Bankruptcy Code, claims should be grouped according to their similarities in classes, divided on a reasonable basis.

Impaired claims: Classes are either unimpaired or impaired. According to **11 USC § 1124 (2)(E)**, an impaired claim or class is when the reorganization plan alters the claim holder's "legal, equitable, and contractual rights". As such, if the payment of the debt is delayed after the effective date of the plan, it is considered impaired.

Entitlement to vote: Only impaired classes have the right to vote. However, the holder of the impaired claim may occasionally not be entitled to vote on a proposed reorganization plan. If all impaired classes were to approve such plans, it could lead to a holdout and prolong the process. Hence, to alleviate possible burdens, a plan does not have to be approved by all impaired classes. Under **11 USC § 1129**, a plan – that meets all other cumulative criteria in the said section - can still be confirmed, despite the existence of potential dissenting impaired classes. As such, the dissenting classes are crammed down.

Cramdown: According to **11 USC § 1129(a)(10)**, a cramdown could only occur if at least one impaired class has voted in favour to accept the plan and the plan does not discriminate unfairly **11 USC § 1129(b)(1)**, and must be fair and equitable to the dissenting classes **11 USC § 1129(b)(2)**.

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Commented [H(21)]: Correct, 1 mark, any one of these aspects is sufficient

Commented [H(22)]: A creditor whose claim will receive nothing is not entitled to vote and is deemed to reject the plan

Question 2.4 (3 marks)

Answer the following questions about preferences, actual fraudulent conveyances and constructive fraudulent conveyances:

(1) Which cause of action applies only to transfers made on account of antecedent debt?

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The Bankruptcy Code provides for a few causes of action (such as claims of preference, actual fraudulent conveyances, constructive fraudulent conveyances) to the trustee or debtor in possession to recover property from pre-petition transferees for the estate.

A transfer may be avoided as a preference. Under 11 USC § 547(b), preferences arise when a transfer of an interest of the debtor is made in property, for a pre-existing or antecedent debt (except when eg it is a contemporaneous exchange of value), to or for the benefit of a creditor, while the debtor was insolvent, made during the suspect period ie 90 days prior to the petition date, that enables the recipient more than it would have in a liquidation procedure under Chapter 7 of the US Bankruptcy Code.

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(2) Which cause of action requires that the debtor be presumed or proven to have been insolvent at the time of the transfer?

All three causes of action – ie preferences under 11 USC § 547(b)(3), actual fraudulent conveyances under 11 USC § 548(a) and (e), and constructive fraudulent conveyances under 11 USC § 548(b) – require the debtor to be insolvent. For the latter two, the debtor may either have been insolvent or may have become insolvent as a result of the transaction.

Commented [H(25)]: Incorrect, while insolvency can be an element of a fraudulent conveyance, but there are scenarios in which a fraudulent conveyance may occur without insolvency (e.g., transaction at undervalue, intentional fraud, etc.)

(3) Which cause of action requires that the debtor be proven to have intended to frustrate creditors' recoveries?

Under 11 USC § 548(a)(1)(A), actual fraudulent conveyances require the debtor to have made the transfer with the intent to "hinder, delay, or defraud" the creditors to which the debtor was indebted to or became indebted. This would be established based on "badges of fraud" as stated under state fraudulent transfer law.

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QUESTION 3 (essay-type questions) [15 marks in total]

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Question 3.1 (3 marks)

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How did *Stern v Marshall* change the law of bankruptcy court jurisdiction and authority to enter a final order?

Bankruptcy courts are created by federal legislation, namely the 1978 Bankruptcy Code. Most other courts are created by the US Constitution under Article III.

The referral statute permits district courts to refer certain proceedings that arise in and relate to bankruptcy proceedings (involving statutory and contractual rights) to bankruptcy courts in their districts, as stipulated under 28 USC § 157 (a). Such proceedings would normally be within the jurisdiction of courts created by Article III under the US Constitution. As such, the US Supreme Court had declared earlier the jurisdictional provisions under the Bankruptcy Code as unconstitutional in the *Northern Pipeline Construction Co v Marathon Pipe Line Co*, 458 US 50 (1982) case.

The referral statute under 28 USC § 157 (b)(1) distinguishes between core matters and non-core matters, stating that the bankruptcy courts are allowed to hear and determine only core matters. Such proceedings are listed, albeit non-exhaustively, under 28 USC § 157 (b)(2). Also, under 28 USC § 157 (c), the bankruptcy court may hear (but not determine) non-core proceedings on the condition that they are sufficiently related to bankruptcy proceedings. The findings of that particular proceeding may be submitted to the district court for its final decision.

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This led to scholars focussing on what could constitute a core or a non-core matter. However, the US Supreme Court ruled in the *Stern v Marshall* 546 US 462 (2011) case that the bankruptcy courts cannot issue final orders within the scope of Article III jurisdiction,

regardless of whether it constitutes a core proceeding. The main question was whether a bankruptcy court could constitutionally determine the case ie enter a final judgment on an otherwise non-core matter presented as a counterclaim.

The *Stern v Marshall* case revolves around a state law counterclaim. Counterclaims by the estate against persons filing claims against the estate are considered core matters under **28 USC § 157(b)(2)(C)**. In this case, the debtor had counterclaimed to the creditor's claim, yet at the same time, the counterclaim was subject to state proceedings, hence interfering with Article III jurisdiction. Although parallel proceedings, in which the first judgment is binding on all parties, is permitted, the state court case continued despite the fact that the bankruptcy judgement was appealed to the district court. The US Supreme Court then ruled that regardless of the fact that the bankruptcy court was allowed to issue a final judgment under the US Bankruptcy Code, this would be unconstitutional over a state law claim under Article III.

As such, this case changed the understanding and rules on bankruptcy courts' jurisdiction and their power to issue a final judgement. It added another layer of complexity, which was later further clarified by other rulings. The bankruptcy courts lacking constitutional authority over a core proceeding may determine by issuing a report and recommendation for review by the district court much like the procedure in non-core proceedings, or the bankruptcy courts may also determine based on the parties' consent.

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Commented [H(31)]: Correct, 1 mark, also the bankruptcy court can rule on a challenge to a petition

Question 3.2 (3 marks)

What provisions of the Bankruptcy Code may not be invoked by a foreign representative in a chapter 15 proceeding? What are two ways that the foreign representative can obtain equivalent relief?

The order for relief under **11 USC § 102(6)** cannot be invoked in a Chapter 15 proceeding. As such, the provision on eg the statutory automatic stay applies under every chapter of the US Bankruptcy Code upon the commencement of proceedings (unless the commencement is being challenged by a motion to dismiss) except under Chapter 15.

The filing of the petition by the foreign representative of the debtor to initiate chapter 15 proceedings does not automatically invoke stay. The stay only takes effect upon granting the petition for recognition of a foreign main proceeding. It is also only limited to the estate that is located within the jurisdiction of the US.

The two ways in which the foreign representative may obtain an **equivalent relief** are either (1) on an interim basis pending such recognition, or (2) following a recognition of a non-main proceeding. According to **11 USC § 1519(a)**, the requirements for recognition are that the foreign representative establishes that a foreign proceeding under **11 USC § 101(23)** is pending and that the representative itself is authorized to act by that proceeding.

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Commented [H(33)]: Incorrect, foreign representatives cannot use statutory avoidance powers. However, they can seek avoidance of transaction under other applicable law or by commencing a plenary proceeding.

Question 3.3 (4 marks)

Describe the differences between interlocutory and final orders and how an appeal may be taken from each. Which courts hear direct appeals from bankruptcy court orders?

There are two sorts of orders in the US non-bankruptcy procedures, namely interlocutory and final orders.

Final orders cover the whole procedure and do not leave any aspect undecided. These orders may be **appealed as of right**, as stipulated under **28 USC § 158(a)(1)**.

Conversely, interlocutory orders resolve parts of the procedure. These may be appealed only **with leave of the appellate court**, as stated in **28 USC § 158(a)(3)**.

According to **28 USC § 158(a)**, the **district courts** have jurisdiction to hear appeals. Another option provided for in **28 USC § 158(b)**, is the **bankruptcy appellate panel** (the

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“BAP”). The BAP is established by the judicial council of a certain circuit, and composes of appointed bankruptcy judges of the districts in the circuit. After the district court or the BAP, a further appeal of right exists for the circuit court of appeals.

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In certain (and rare) circumstances, an appeal from the bankruptcy court may “skip” the BAP or district court and make use of the right to **directly appeal to the circuit court of appeals**. However, under **28 USC § 158(d)(2)(A)**, such appeals should be certified by the bankruptcy court that it meets one of the following criteria: (1) the appeal concerns a question of law which has not been answered yet by the circuit or the US Supreme Court, (2) the appeal concerns a question of law that requires a resolution between conflicting answers, or (3) if the direct appeal would materially progress the case.

Question 3.4 (5 marks)

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What fiduciary duties do directors of Delaware corporations owe and to whom are the duties owed in the ordinary course of business? To whom are duties owed when the corporation is potentially or actually insolvent?

Directors’ liabilities are matters of state law of the state of incorporation. In the case of Delaware, directors owe a **fiduciary duty of loyalty to the corporation’s best interest** and a **duty of care** (which also include the basic fiduciary duties of good faith, oversight, and disclosure).

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Commented [H(43)]: Correct, 1 mark

The duty of care necessitates informed decision-making by the directors based on all reasonably available information, and the duty of loyalty requires the directors to act based on an independent (ie directors should have no relationship with an involved party which is influential to its decision-making and should not financially benefit from a decision) and good faith manner, with an honest belief that this would be in the best interests of the corporation and its shareholders.

Such duties are owed to the **corporation and its shareholders** both in the **ordinary course of business** and when a corporation is operating in the zone of **insolvency** or is insolvent. The directors do not owe any duties to creditors.

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As a side note, compliance with duties are reviewed and evaluated by courts in Delaware under the test of the **business judgement rule**. The test commences with a rebuttable presumption that directors comply with their fiduciary duties. A counterparty has the burden of proof to rebut this presumption. It needs to produce evidence that the directors were acting with **gross negligence** as they were insufficiently informed or made decisions with interests in mind other than that of the corporation. It is important to note that the directors will not be held liable for gross negligence unless the presumption is rebutted.

QUESTION 4 (fact-based application-type question) [15 marks in total]

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Question 4.1 [4 marks]

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Gambling Corporation is incorporated and has a principal place of business in Greece and it operates casinos and betting parlors in many international cities, including Athens, Las Vegas, London and Macau. Gambling Corp’s bonds (governed by English law) are due to mature in one (1) year, but it is unable to repay or refinance them. Gambling Corp is considering using an English scheme of arrangement to restructure the bonds.

Discuss whether the English scheme of arrangement could be granted recognition under US chapter 15 as a foreign main or foreign non-main proceeding.

To determine whether the English scheme of arrangement could be granted recognition under US Chapter 15 – and more specifically under **11 USC § 1517** – it is important to first distinguish between a foreign main and a foreign non-main proceeding.

A **foreign main proceeding** requires the debtor's **centre of main interests (COMI)** to be located in the territory where the proceedings are commenced. According to Article 3 of the **UNCITRAL Model Law on Cross-Border Insolvency (MLCBI)** and **11 USC § 1502 (4)** such a proceeding is a foreign proceeding pending in the country where the debtor has the COMI. Only if it satisfies this definition, it can be granted recognition as a foreign main proceeding under **11 USC § 1517(b)(1)**. The **MLCBI** – which has been adopted as **Chapter 15** of the US Bankruptcy Code – provides a rebuttable presumption, namely that the COMI is the place of incorporation. **11 USC § 1516(c)** stipulates that, in the absence of evidence to the contrary, the COMI is presumed to be the debtor's registered office. According to *In re Sphinx Ltd*, 351 BR 103, 117 (Bankr SDNY 2006), the relevant factors to take into account when determining a debtor's COMI are the locations of the HQ, management, primary assets, majority of the debtor's affected creditors, applicable jurisdiction to the majority of disputes of the case. The COMI should be readily ascertainable by third parties on the basis of objective factors (see also *Morning Mist Holdings Ltd v Kryss (In re Fairfield Sentry Ltd)* 714 F.3d 127).

Taking all of this into consideration, the Gambling Corporation COMI should be presumed to be located in Greece as it is incorporated and has its principal place of business situated in that territory. Given from the facts of the case, there is no reason to rebut this presumption. As such, since the COMI is not located in the United Kingdom, it cannot be stated that the proceeding commenced in that territory fulfils the criteria of a foreign main proceeding.

According to **11 USC § 1502 (5)** a **foreign nonmain proceeding** means a foreign proceeding, other than a foreign main proceeding, pending in a country where the debtor has an **establishment**. If a proceeding fulfils this definition, it may be granted recognition as a foreign non-main proceeding under **11 USC § 1517(b)(2)**. An establishment is defined as any place of operations where the debtor carries out a non-transitory economic activity (see **11 USC § 1502 (2)** and *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund* 374 BR 122 (Bankr SDNY 2007)).

As the Gambling Corporation operates casinos and betting parlors in many countries among which London, the English scheme of arrangement procedure could be recognized as a foreign non main proceeding under Chapter 15.

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Question 4.2 [5 marks]

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Oil Corporation is incorporated in Delaware and has its principal place of business in Texas. Oil Corp is facing a number of challenges to its business. First, ShipCo, one of its key customers, has filed a breach of contract lawsuit in Texas state court alleging that Oil Corp sold it contaminated oil that caused USD 1 billion in damage to ShipCo's container ships. Second, the US Department of Justice is investigating whether Oil Corp illegally purchased oil from countries subject to US sanctions. Third, Oil Corp. has missed a payment on its secured loan from USA Bank, and USA Bank is threatening to foreclose on an Oil Corp refinery located in the Philippines. Fourth, because of all these distractions, Oil Corp has forgotten to pay rent on its Houston, Texas office space and its landlord is threatening to evict it. What would be the effect of Oil Corp filing a chapter 11 petition on each of these four situations?

Upon filing a bankruptcy proceeding under any chapter – except Chapter 15 – of the Bankruptcy Code, including Chapter 11, a **worldwide automatic stay under 11 USC § 362** becomes immediately effective in order to protect the property of the debtor's estate from individual creditor enforcement actions with regard to prepetition claims. This provides the debtor with a breathing room to formulate a reorganization plan. The scope of this stay is very broad. However, certain exceptions apply. The effects of filing a Chapter 11 petition on the four situations will be assessed below.

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ShipCo has filed a breach of contract lawsuit in Texas state court alleging that Oil Corp sold it contaminated oil that caused USD 1 billion in damage to ShipCo's container ships. Hence, ShipCo has filed a lawsuit against the debtor for breach of contract. This would be a continuation of litigation on pre-petition claims, which is **prohibited under 11 USC § 362(a)(1)**. As such, **the stay will also affect and stay the proceedings initiated by ShipCo.**

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The US Department of Justice is investigating whether Oil Corp illegally purchased oil from countries subject to US sanctions. This investigation is part of a regulatory investigation. Under **11 USC § 362(b)(4)**, the stay does not affect such investigations as they constitute statutory exceptions. As such, **the investigation will not be effected by the petition.**

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Oil Corp has missed a payment on its secured loan from USA Bank, and USA Bank is threatening to foreclose on an Oil Corp refinery located in the Philippines. However, when the petition is filed, this will be under the list of prohibited interferences with the property of the estate in any part of the world. According to **11 USC § 362(a)(3)** any act to obtain possession of property of the to exercise control over it is not permitted. As such, the USA Bank's action to control Oil Corp's Filipino refineries **will be barred.**

Commented [H(57)]: Correct, 1 mark

Oil Corp has forgotten to pay rent on its Houston, Texas office space and its landlord is threatening to evict it. This action by the landlord falls under one of the statutory exceptions of the stay. **11 USC § 362(b)(23)** allows the eviction of a debtor-tenant from property that is non-residential if the lease is expired after the filing of the petition. If the lease is indeed expired, the landlord of the office space in Texas may evict Oil Corp for it is not a residential property and it **falls under the exception of the stay.**

Commented [H(58)]: Here, there's no reason to believe the lease is expired, so eviction would be stayed

Question 4.3 [6 marks]

Commented [H(59)]: Total marks 5/6

Oil Corp has filed for bankruptcy and is planning to sell its plastic manufacturing business through a 363 sale. The plastic manufacturing business operates under the trademark "Interconnect", which is licensed from Plastic Corp. Oil Corp has invented several patented processes for plastic manufacturing, which it licenses to Plastic Corp. The main manufacturing facility for the plastic business is in Dallas, and Oil Corp has granted a lien on the facility to USA Bank to secure its USD 500 million loan.

Oil Corp thinks it will get the highest return for the plastics manufacturing business if it can (i) assume and assign the trademark license; (ii) reject the patent licenses so the purchaser has the exclusive right to use the patents; and (iii) sell the manufacturing facility free and clear of the USA Bank lien. Can Oil Corp achieve each of these goals without the consent of Plastic Corp and USA Bank? Why or why not?

These questions concern dealings with properties of the estate during a bankruptcy proceeding. The scope of the powers of Oil Corp depends on whether it concerns a transaction done in the ordinary course of the business and whether there are any interests affected by the transaction. The three separate scenarios will be discussed below.

Firstly, it should be determined whether Oil Corp can assume and assign the trademark license, and how. It is important to note that this concerns an executory contract. However **this license cannot be assumed and assigned without licensor consent (see *In re Trump Entertainment Resorts Inc* 526 BR 116 (Bankr D Del 2015)). As such, the consent of Plastic Corp is required.** USA Bank is not involved in this contract, hence its consent is not needed.

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Commented [H(61)]: Correct, 1 mark

Secondly, according to **11 USC § 365(n)(1)** licensees of patents owned by the debtor are protected, meaning that **the licenses may not be terminated with its sale without consent.** As such, if the contract is rejected under which the debtor is a licensor of a right to a patent (ie an intellectual property), the licensee under such contract may elect to treat such contract as terminated. Patents owned by Oil Corp cannot be terminated in connection with the sale of the intellectual property without consent of Oil Corp. Hence, **the consent of Plastic Corp is not needed.** Again, USA Bank is not involved in this contract; its consent is therefore not needed.

Commented [H(62)]: Correct, 1 mark

Commented [H(63)]: Incorrect, for the purchaser of the patents to have exclusivity, Plastic Corp's consent would be required

Thirdly, to determine whether Oil Corp may sell the manufacturing facility free and clear of the USA Bank lien with or without its consent, it is important to first discuss a **363 sale**. As the name suggests, this sale is codified in **11 USC § 363** on the use, sale, or lease of property. During the reorganization procedure, the debtor has – thanks to the stay – a breathing space, to deal with its property without creditor interference and can sell its property free and clear of creditors' claims with the approval of the court and creditor's consent where its interest is disputed or where the value of the property exceeds the value of the interests, **11 USC § 363(f)(2)**. The creditor will then attach its interests to the sale's outcome with priority in its distribution. A 363 sale with consent is the ideal way for the debtor to sell its assets free and clear of liens and other interests. In such instances, all parties with an interest in the property have agreed to the terms of the sale. Moreover, **11 USC § 363(f)(5)** stipulates that the property may be sold free and clear without consent of the creditor if the payment is made to the creditor in a value equal to its interest. The bank would have to be compelled to accept a money satisfaction of such interest. Another way is **11 USC § 363(f)(3)**, according to which no consent is needed if such interest is a lien, and the price at which such property is sold would be greater than the aggregate value of all liens on such property. Depending on whether the Bank's interests are disputed or whether the property's value exceeds the value of the interests, Oil Corp may or may not need the Bank's consent. These issues cannot be deducted from the facts of the case which may indicate that such a situation does not exist. Hence, one would argue that **the consent of USA Bank is not needed**. The consent of Plastic Corp is not needed as it is not involved in the case.

Commented [H(64)]: Correct, 1 mark

Commented [H(65)]: Correct, 1 mark

*** End of Assessment ***